

Income tax: restriction of relief for losses in farming or market gardening

Part 23-01-05

This document should be read in conjunction with section 662 of the Taxes Consolidation Act 1997

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Introduction

This manual outlines the circumstances in which section 662 of the Taxes Consolidation Act 1997 ("TCA 1997") restricts relief for losses incurred in a trade of farming or market gardening.

1. Circumstances in which loss relief is restricted

A person who incurs a loss in a tax year in a trade of farming or market gardening is entitled to relief from income tax under section 381 TCA 1997.¹ This relief (including any amount in respect of allowances which by virtue of section 392 TCA 1997 is to be treated as a loss) is restricted by section 662 TCA 1997 as follows:

- The relief is not available unless it is shown that the loss was incurred in a year when the trade was carried out on a commercial basis and with a view to the realisation of profits (section 662(2)(a) TCA 1997).
- The relief is not available if in each of the three preceding years a loss was incurred in carrying out that trade (section 662(2)(b) TCA 1997).

These restrictions are applied independently of each other. This means, for example, that even if in the year a loss was incurred the trade was carried out on a commercial basis and with a view to the realisation of profits, relief will not be available if a loss was incurred in each of the three preceding years.

2. Expectation of profit

The object of section 662 TCA 1997 is to deny income tax relief to "hobby" farmers and market gardeners. It is not aimed at farmers and market gardeners who are genuinely trading. Accordingly, section 662(2)(c) TCA 1997 provides that the fact that a trade is conducted so as to afford a reasonable expectation of profit is to be conclusive evidence that it was being carried on with a view to the realisation of profits.

¹ For guidance in relation to loss relief, please refer to Revenue's [Notes for Guidance](#).

3. Potential for making profit

The strict application of section 662 TCA 1997 is further modified by section 662(2)(d) TCA 1997, which provides that relief is not to be denied if it can be shown that:

- (a) the whole farming or market-gardening activities in the tax year of claim are of such a nature, and carried on in such a way as would have justified a reasonable expectation of the realisation of profits in the future if they had been undertaken by a competent farmer or market gardener, and
- (b) if such competent farmer or market gardener had undertaken those activities at the beginning of the "prior period of loss"², such farmer or market gardener could not reasonably have expected those activities to become profitable until after the end of the year following the prior period of loss.

The exception provided by subsection (2)(d) is designed to apply to genuine farmers or market gardeners carrying on a special kind of undertaking which is potentially profit-making but cannot be expected to show a profit before the end of the tax year of claim. For instance, it might take three years (or more) to regenerate marginal land or to build up a stud farm.

Where a claimant relies on section 662(2)(d) TCA 1997, the whole farming or market gardening activities are to be taken into consideration.

The onus of proof is laid entirely on the claimant who must show that the nature of activities is such as to provide a reasonable expectation of profit in the future. Any activities which, however, efficiently carried on, could never show a profit, do not qualify. In addition, the claimant must show that the activities are carried on in a competent manner with a reasonable expectation of profit. To satisfy the condition set out in paragraph (b) above, the farmer should produce evidence as to the normal period of years during which a competent farmer or market gardener, engaged in the same type of long-term farming or market gardening activity, would be expected to show initial losses before his or her operations reached a profit-making level.

Any case in which relief is claimed under section 662(2)(d) TCA 1997 will be considered on its own merits.

² Subsection (1) defines the "prior period of loss" as, in effect, the last three years before the beginning of the tax year of claim plus any earlier periods which together with those three years make up a consecutive loss-making sequence.

4. Ancillary to a larger trade

Section 662(2)(e) TCA 1997 provides that relief is not to be denied where the loss-making farm or market garden is part of, and ancillary to, a larger trading undertaking. A close operating link with and a contribution to the larger undertaking is required. This provision is designed to meet cases such as that of a person who rears cattle to supply his meat trade.

5. Commenced within three years

Section 662(5) TCA 1997 provides that the loss relief restriction does not apply where a trade was set up and commenced in the three years preceding the year of claim. For these purposes, a trade shall be treated as discontinued and a new trade set up in any event which, under the Income Tax Acts, is to be treated as equivalent to the permanent discontinuance or setting up of a trade. For example, the sale of a farm by one person to another.

6. Anti-avoidance

As an anti-avoidance measure, where a trade of farming or market gardening changes hands, the relief does not apply if the persons carrying on the trade immediately before and immediately after the change are connected.³

7. Carry forward

The carry-forward of losses incurred in farming or market gardening is not restricted by section 662 TCA 1997. Therefore, a farmer who suffers losses for a number of years is still entitled to carry forward all unused farming losses under section 382 TCA 1997 for use against farming profits of subsequent periods.

8. Burden of loans

Many farmers, otherwise carrying on farming on a commercial basis and with a view to making profits, are incurring losses over prolonged periods due to the burden of loans entered into at a time when the state of the market and the prevailing rates of interest suggested that sufficient profits could be generated to service the loans. These loans can now be serviced only by the farmer or his spouse either obtaining an alternative source of income or diverting income from an existing source.

³ For guidance in relation to connected persons, please refer to Revenue's [Notes for Guidance](#) (pages 15-17).

In the circumstances, if there is proof:

a) that farming is being carried out on a commercial basis and with a view to the realisation of profits and that profits would have resulted but for the existence of the loans, and

b) that genuine efforts are being made to meet the interest payments on the loans,

then relief may be allowed for the losses in the fourth and subsequent years under section 381 TCA 1997.

The mere debiting of interest payments to a current or other account should not be accepted as proof that the interest payments are being met. There must be a genuine diverting of income from another source to meet the interest and relief should be allowed only to the extent that interest has actually been paid. In the case of a term loan the amount of interest paid can be determined by reference to the actual payments made on the loan. In the case of a current account or a term loan which is debited to a current account the amount paid may be determined by comparing the opening and closing balances. If the closing balance does not exceed the opening balance, it may be accepted that all the interest debited has been paid or if it exceeds the opening balance by an amount which is less than the interest debited, the difference between the excess and the interest debited may be taken as having been paid.

Where accumulated interest is subsequently paid by disposing of land or otherwise, the accounts for prior years may be re-opened, subject to the four-year time limit, so as to allow any section 381 relief which would have been allowed if the interest had been paid.⁴

⁴ For guidance in relation to the four-year time limit, please refer to paragraph 5 of Tax and Duty Manual [Part 37-00-30 Repayments and Offsets of Taxes](#) .